

**IN THE MATTER OF THE APPLICATION REGARDING CONVERSION
OF PREMIERA BLUE CROSS AND ITS AFFILIATES**

Washington State Insurance Commissioner's Docket # G02-45

REPORT OF

Towers Perrin

Review of Premiera's Executive Compensation Program

November 7, 2003

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PREMERA

Review of Executive Compensation Program

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TABLE OF CONTENTS

EXECUTIVE SUMMARY

INTRODUCTION

I. PREMERA COMPENSATION

II. PRICEWATERHOUSECOOPERS REPORT

III. POST-CONVERSION COMPENSATION

APPENDIX

- Towers Perrin Competitive Pricing Process
- Mercer Competitive Pricing Process
- PricewaterhouseCoopers Pricing Process
- Competitive Pricing Analyses
 - Comparison to Mercer
 - Comparison to PwC

EXECUTIVE SUMMARY

The proposed conversion of PREMERA, Premera Blue Cross, and certain of their affiliates (collectively, "PREMERA" or the "Company") from a non-profit to a for-profit company is being reviewed by the Washington Office of the Insurance Commissioner ("Commissioner"). In connection with this review, PricewaterhouseCoopers LLP ("PwC") was retained by the staff of the Washington Office of the Insurance Commissioner ("OIC Staff") to review matters related to PREMERA's executive compensation practices.

To further assist in the Commissioner's review, PREMERA's attorneys have requested that Towers Perrin conduct an independent analysis of the Company's current and planned future executive compensation practices, including our assessment of the work performed by PREMERA's compensation consultant Mercer Human Resource Consulting Inc. ("Mercer"), and the PwC Report.

Towers Perrin is a leading human resources consulting organization, with one of the largest executive compensation practices in our industry. We have not performed executive compensation consulting work for PREMERA since 1998.

Approach

As detailed in this report, we have reviewed the written reports of PwC and the Mercer reports prepared for the Company that PwC reviewed, and interviewed certain senior PREMERA executives and directors on its Board. We conducted our own determination of competitive compensation levels for senior PREMERA executives in light of market practices, the Company's alignment of responsibilities and its compensation philosophy and strategy.

Our review focused on *direct compensation* (salary, annual bonus, long-term incentives, and elements of the change-in-control protection arrangements). We have also reviewed PwC's comments regarding the non-qualified retirement programs.

Towers Perrin Conclusions

I. Current Compensation Program

Towers Perrin assessed the executive compensation program of PREMERA from what we consider to be four critical aspects of sound business practice: reasonableness and appropriateness of the compensation philosophy, the involvement of the board of directors in executive compensation, the relationship between the Company and its compensation consultant (i.e., Mercer), and the reasonableness and appropriateness of compensation levels.

In our opinion, based on information we have reviewed, PREMERA's program is reasonable and appropriate in philosophy, design, administration, and compensation levels as the following aspects of the compensation program demonstrate.

- Towers Perrin concludes that PREMERA's executive compensation philosophy is conservative and reasonable for a company in its industry, and that the philosophy appears to guide the design, implementation and administration of the compensation program in the past and post conversion.
- The compensation philosophy specifies that the competitive market for compensation purposes will be public and private (non-profit) health insurers, which represents companies that PREMERA recruits from and can lose talent to. Data from this market will be adjusted to reflect PREMERA's relative size.
- Target compensation level is the median of the peer group when target performance is achieved, except when circumstances require extraordinary skill levels. Jobs will be benchmarked to the market to take into account PREMERA's alignment of responsibilities.
- Incentive objectives are set based on the Company's strategy, specific business conditions and requirements, and overall industry performance.
- Based on our interviews and study of written material provided to us, it appears that the PREMERA Board of Directors and the Compensation Committee exercise a degree of oversight that is consistent with the trend towards active and independent governance practices among U.S. corporations.
- The Board, through its Compensation Committee exercises active involvement in the design and administration of the executive compensation program including selection of performance measures and targets, and determination of pay levels for new hires and incumbent executives.
- Mercer maintains an active and independent relationship with the Compensation Committee, meeting frequently without management present, and communicating directly with members of the Committee.
- Mercer conducted market analyses using techniques generally similar to those we use in our analyses, and their determination of market pay levels are generally similar to our independent analysis. We believe this is healthy and consistent with best practices.

II. PwC Report

Towers Perrin reviewed the PwC conclusions as they relate both to level of pay (*how much*) and plan design (*how pay is delivered*). Although the Report was critical of many aspects of PREMERA's program, our analysis focused on statements that in our opinion represent the most significant concerns.

■ Level of Compensation

The PwC Report concluded that compensation in the aggregate and for most senior executives is significantly above the market median. Towers Perrin disagrees with this, except in the case of a single executive (now retired) who was hired in order to obtain a high level of very specific skills. We found that total direct compensation is at or below the market median in the aggregate and in all but a very few individual cases. Our reasons for differing from PwC are:

- We do not agree with certain of the PwC analytical techniques as we understand them; these resulted in lower levels of market compensation
- We do not believe that the standalone comparisons with the Blue Cross Blue Shield industry are relevant. We concur with PREMERA's view that this *segment* of the industry per se is not an appropriate peer group.
- PwC did not seem to take PREMERA's unique organizational alignments into account. Specifically, as PREMERA does not have a Chief Operating Officer, the duties of this position are shared among several top executives.
- In our opinion, PwC uses an arbitrary and flawed approach to measure performance among Blue Cross Blue Shield companies to support a conclusion that PREMERA's comparative performance does not justify compensation delivered.
- PwC's criticism of salary increases does not take into account the Company's or the specific incumbents' (e.g., external hire, internal promotion) circumstances.

■ Form of Compensation

The PwC Report concludes that all of PREMERA's compensation and benefit programs are "at or above market practice." Towers Perrin disagrees with this conclusion. In our opinion the direct compensation programs are in the mainstream of those provided by the appropriate peer group, and as stated

earlier are administered to deliver compensation that is at the market median except as noted previously. Where specific plans have certain features that may be unusual, they are offset to ensure that pay delivered is appropriate. Specifically:

- PwC criticized the use of ending salary to calculate the long-term incentive rather than the salary at the beginning of a cycle. Towers Perrin finds that about half of major companies use this practice, and further that PREMERA's formula ensures that awards will be at market levels.
- We do not concur that the protection provided to PREMERA executives in the event of termination following a change-in-control is more generous than market practice.
- We do not agree that PREMERA uses an inappropriately high weighting (i.e., 40%) on non-financial measures for the annual bonus plan. In the first place, PREMERA's plan is in fact funded *entirely* by financial measures, and subsequently may be reduced by other measures, as much as 40%. Furthermore we believe that non-financial measures (e.g., service, quality) are critical for a health insurer and must receive significant emphasis.

III. Post-Conversion

The PwC Report is critical of the latitude allowed to PREMERA under the Exhibit G-10 to the Form A. Since the PwC Report was filed, PREMERA submitted additional information on its stock plans, which we have reviewed.

Towers Perrin does not believe that the proposals and commitments PREMERA has made are either unreasonable or generous. On the contrary, we believe that these are in the mainstream of competitive practice at an IPO, and believe they provide the Board with adequate flexibility to grant competitive equity-based awards which will align the interests of management with those of shareholders, without unjustly enriching management or causing excessive shareholder dilution.

INTRODUCTION

PREMERA is a non-profit holding company based in Washington, the affiliates of which include Premera Blue Cross. The PREMERA family of companies offers life and health insurance and related services. PREMERA has applied to the Washington Office of the Insurance Commissioner in regard to PREMERA's conversion to a for-profit corporation followed by an initial public offering.

In connection with the proposed conversion, PREMERA's current and proposed executive compensation programs have been reviewed by PwC, a compensation consulting organization engaged by the OIC staff.

Towers Perrin is an international firm of management consultants and actuaries. We assist client companies in evaluating, designing, communicating and administering human resources programs, including direct compensation, benefits, and retirement programs. Our staff comprises over 9,000 in about 79 offices worldwide. Towers Perrin has not worked with PREMERA on the design of direct compensation programs for the last 5 years.

PREMERA's attorneys have asked Towers Perrin to assist in several areas:

- I. Compensation Program. Review and evaluate PREMERA's compensation philosophy and the methodology, reports, recommendations and analyses presented by Mercer Human Resource Consulting Inc. ("Mercer") to the compensation committee of the PREMERA Board of Directors.
- II. PwC Report. Review and evaluate the Executive Compensation Report prepared by PwC for the OIC Staff.
- III. Post-Conversion Program. Review and evaluate PREMERA's Proposed Reorganization/Equity Incentive Plan and the relevant portions of the Blackstone Group's Report on Evaluation and Fairness of the Proposed Conversion, dated October 27, 2003 for the OIC Staff with respect to stock plans.

This report is organized to address each of the above subjects, with an appendix that details Towers Perrin's determination of appropriate market compensation levels for selected positions and comparison of our approach with that of Mercer and PwC.



I. PREMERA COMPENSATION

Towers Perrin reviewed the PREMERA compensation philosophy and program through interviews with members of the Board of Directors, line and staff executives of PREMERA, and Mercer Consultants. We have also reviewed the written material made available to PwC and OIC. The following conclusions are based on our interpretations of the interviews, our analysis of the written material, and our own data and experience.

A. Compensation Philosophy

PREMERA has articulated and adopted an executive compensation philosophy which was approved by the Governance Committee of the Board of Directors, which formerly was responsible for management compensation, and now by the Compensation Committee as well as by the Board. We understand that the key elements of the philosophy include the following:

- Compensation opportunities will be set at the median of the company's peer group for achieving target results except in extraordinary cases where particular individual skill, talent or experience is needed, and demonstrated by the incumbent, requiring above-median compensation.
- Market compensation for individual positions will be determined according to PREMERA's mix of management responsibilities, not solely by industry job definitions.
- Peer companies include the entire health insurance industry, including publicly-owned, private, and not-for-profit organizations of appropriate size.
- Performance measures and objectives will be set at rigorous but achievable levels and will include financial measures that reflect the Company's financial health, strategic measures related to continuing future financial soundness, and measures that reflect PREMERA's market and operational objectives such as service and quality.

* * *

Conclusion:

Towers Perrin concludes that PREMERA's executive compensation philosophy is conservative and reasonable for a company in its industry, and that the philosophy appears to guide the design, implementation and administration of the compensation program in the past and post conversion.

B. Board Involvement

Towers Perrin understands that the Compensation Committee (and in certain matters the entire board) is actively involved in the design, review and administration of the compensation program. This includes setting performance objectives, monitoring compensation levels vs. market practices, determining the reference market and reviewing (and if applicable, approving) compensation levels as required. The Compensation Committee meets in executive session to review and approve, among other things, incentive awards. The Committee has direct, frequent access to the Company's compensation consultant, Mercer, including meetings in executive session. We also understand that the PREMERA board has generally followed many of the practices and principles of Sarbanes-Oxley, although not required to do so as a not-for-profit private company.

The diverse background of the individual directors, the reported active commitment of each director, and the overall impact of the board on PREMERA's compensation program appears highly positive.

* * *

Conclusion:

Based on our interviews and study of written material provided to us, it appears that the PREMERA Board of Directors and the Compensation Committee exercise a degree of oversight that is consistent with the trend towards active and independent governance practices among U.S. corporations.

C. Compensation Consultant

The PREMERA Compensation Committee currently engages Mercer as the Company's executive compensation consultant. Towers Perrin has reviewed Mercer reports to the Compensation Committee of the Board, and we have also conducted our own analyses of competitive compensation levels for selected positions. As shown in the appendix to this report, our results are not substantially different from those of Mercer, although variations occur because of different survey data and different techniques that each of our firms has adopted.

In our independent review of the process that Mercer used to determine benchmark positions to compare to PREMERA positions we believe a proper accounting was provided. Factors such as the incumbents' roles and responsibilities and the current strategic priorities of PREMERA along with the associated skill, talent and responsibility demands needed to achieve the strategy were incorporated. As well, we find that Mercer developed a peer group

that reflects the local and national competitive market for talent in the broad healthcare insurer industry. Further, pay strategy and performance measurement have evolved appropriately with PREMERA's financial situations, from fiscal distress, to turnaround, to financial stability.

* * *

Conclusion:

Our overall assessment of the consulting relationship, derived from interviews with Mercer, PREMERA management and directors, plus a review of Mercer's reports and letters is that the relationship is a healthy one, characterized by an active direct dialog with, and responsibility to the board of directors.

II. PRICEWATERHOUSECOOPERS REPORT

PWC EXECUTIVE COMPENSATION REVIEW: COMPETITIVENESS AND REASONABLENESS OF PREMIER PRACTICES ("PwC REPORT")

The PwC Report dated October 2003 was conducted at the request of the OIC staff with the stated primary objectives of determining if the conversion to a publicly-held company would unjustly enrich certain employees, if the executive compensation and benefit practices of PREMIER are consistent with "best practices" in the industry, and if the conversion is necessary for strengthening the Company's employee retention.

We have not specifically commented on the subject of the necessity of conversion to strengthen the Company's employee retention, as this is a determination that we believe only senior management and the Board is in a position to make. Further, we understand that retention of senior executives is not an issue that is of particular concern at present.

The PwC Report cited a number of areas in which PREMIER's executive compensation levels and programs are "above market practice." In order to provide our opinions on the report most clearly, we have grouped the conclusions regarding "above market practice" in two categories: **A) pay levels** (how *much* compensation was delivered to executives) and **B) program design** (how pay is delivered). For each, we consider pre-conversion and post-conversion.

We have limited our responses to what we consider to be the most significant areas of concern regarding current and future compensation. (We would be happy to discuss any additional aspects of the PwC Report that the Commissioner deems necessary and appropriate.)

PwC REPORT OBSERVATIONS AND TOWERS PERRIN RESPONSES

A) Pre-Conversion – Pay Levels

1. *PwC states that: "TDC [Total Direct Compensation] provided to PREMIER's Top Five and SVPs is above market practice" (page 7)*

Towers Perrin Response:

- PwC does not explain how market total direct compensation levels (salary, annual bonus, and long-term incentives) were determined for individual positions. The exhibit titled "Total Direct Compensation: Executives (Top 5)" in Appendix B of the PwC Report shows salary plus bonus only. However, in Appendix A the report states that data from the Survey Group was used with a "discount rate of 40%" applied to survey-reported long-term compensation to account for PREMIER's inability to grant stock. Because the survey group contains not-for-

profit companies as well as public companies, and all are viewed as peers, Towers Perrin does not understand or agree with the use of such a discount, which would substantially reduce the apparent market level of TDC. This discount:

- Does not distinguish between stock and non-stock companies
- Ignores the assertion that PREMERA has recruited from stock companies as well as not-for-profits/non-profits
- Management and Board members have articulated a compensation philosophy of targeting median compensation except when special skills are needed for particular jobs, or when responsibilities exceed those usually found for a particular position in the industry.

Further, PREMERA appropriately considers its peers to be the health insurance industry, including both for-profit and not-for-profit companies, and does not view the Blue Cross Blue Shield industry as the sole source of talent or competitors for executives.

Finally, PREMERA has adopted a performance-based compensation system that is based on a strategy developed as the present management team was put in place and turned the company around after a multi-year period of substantial financial losses. Performance is measured and goals are set based on what the Company needs to accomplish *strategically* to deliver quality services to its constituencies, and *financially* to ensure continuing growth in profits and financial stability from the serious losses incurred in the late 1990s.

- In the PwC Report, some of the executive positions were apparently priced primarily according to a generic title that did not take into account either their extra responsibilities or the Company's particular needs.

In particular, PREMERA has no COO, and many of the duties of this position have been assigned to the EVP/Chief Legal and Public Policy Officer. PwC appears to have priced this position as a "Top Legal Executive," with little consideration given to the extensive additional responsibilities of this position, including human resources, external and internal communications, government affairs, compliance, business continuity and disaster recovery, and regulatory affairs.

Accordingly, Towers Perrin would categorize this expanded role as a Chief Administrative Officer and price this position at \$800,000 for total direct compensation at the median for the health insurance industry (vs. the PwC level of \$499,580), resulting in actual pay of 4% below median market. (See the Appendix.)

- The Chief Actuary position was also apparently priced by PwC primarily according to the title, with little consideration given to the primary responsibility of developing and implementing the "B&ST", a major initiative for PREMERA, in addition to maintaining his position as Chief Actuary. (The incumbent retired in 2003; the new Chief Actuary is paid at a lower SVP level.)

It should also be noted that this incumbent was recruited from a senior position at a public company, at a compensation level deemed necessary to acquire his skills to fill a critical set of requirements.

Towers Perrin would price the position at \$490,000 median total direct compensation (vs. the \$414,000 of PwC), resulting in actual pay of 36% over median, which is consistent with the Company's intention to pay above "median" for extraordinary skills. (See the Appendix.)

- With these two positions removed from PwC's top 5 analysis, the resulting actual total TDC is \$2.805 million vs. PwC median Health Insurance Industry total of \$2.719 million, or a difference of 3%.
2. PwC states that: *"Actual TCC for the Top Five Executives for 2002 is at the 75th percentile of competitive practice whereas PREMERA's relative performance score is at the 38th percentile" (page 14)*

Towers Perrin Response:

- PwC uses a method to compare performance of Blue Cross Blue Shield organizations to PREMERA's performance based on three measures:
 - Premium growth
 - Absolute dollar operating income
 - Operating margin

These measures are used by PwC both in annual and long-term performance measurement, but weighted differently. It is not clear to Towers Perrin why an absolute level of income based on a 15-company peer group is relevant to either annual or long-term performance, as this simply defines company size.

More fundamentally, Towers Perrin observes that most companies – including PREMERA – base their annual incentive plans on the achievement of objectives that are relevant to their strategy, local market conditions, etc. Comparing annual performance for all companies in a peer group on the same basis is highly unusual for annual incentive plan purposes and Towers Perrin believes

that the analysis is not relevant to, nor appropriate for, an assessment of compensation levels.

3. ***PwC states that: "From 1998 through 2002, salaries at PREMERA grew faster than market rates of approximately 4% per year" (page 7)***

Towers Perrin Response:

- Companies generally adjust salary levels of their most senior executives to accommodate changes in responsibilities and contribution.

Several of PREMERA's senior executives were new to the company or to their positions in the late 1990s, and as they progressed in their level of performance, and the scope of their responsibilities was increased, the board approved salary increases that may have been above overall company merit budgets.

Towers Perrin considers aggregate pay vs. market to be a relevant measure in this case, more so than historical rate of increase.

* * *

Conclusion:

In our opinion, the overall thrust of the PwC Report regarding current levels of executive compensation was that they are unreasonably high. Towers Perrin believes that the techniques and approaches used by PwC did not take PREMERA's philosophy or organization into account, and further we disagree with the PwC interpretation of market data and their analysis of performance of PREMERA and other Blue Cross Blue Shield companies. Towers Perrin's analysis has shown that PREMERA's executive compensation levels are reasonable.

B) Plan Design

The PwC report states that "PREMERA has generally implemented above market practices in comparison to similarly sized Blue Cross Blue Shield organizations." As stated previously, PREMERA has determined that the health insurance sector is the peer group, not the more narrowly defined Blue Cross Blue Shield segment. Nonetheless, Towers Perrin has the following comments on specific elements of the PwC Report.

1. **PwC states that: "PREMERA calculated LTI payouts based on salary at the end of the cycle versus at the time of award/grant. This is unusual and generous compared with typical practice." (page 8)**

Towers Perrin response:

- Towers Perrin disagrees with the PwC characterization of the practice as "unusual" based on our Long-Term Incentive Plan design survey which shows 43% of companies incorporate ending salary. We generally recommend that clients base LTI on beginning salary mainly for ease of administration and to mitigate the leverage impact of salary increases.

Further, the practice is not necessarily *generous*, as the actual payout depends also on the bonus as a percentage of salary. In PREMERA's case, the target bonus percentages tend to be lower than market, resulting in total compensation at or below market.


2. **PwC states that: "The level of CIC protection provided to the CEO, EVPs and SVPs within PREMERA's CIC policy is quite comparable, and, in some instances, better than that provided by publicly-held organizations and more competitive than practices found in not-for-profit organizations." (page 12)**

Towers Perrin Response

- Towers Perrin has observed that CIC arrangements for not-for-profit organizations parallel those of for-profit companies. Accordingly, the differences that PwC refers to between the two classes of company are not clear to us.
- The multiples of salary and incentives provided by PREMERA upon a covered termination following CIC are comparable with practices across industries, in our experience.
- PREMERA's plan does not include long-term awards in the benefit multiple; some not-for-profit organizations include LTIP in order to provide a benefit more comparable to stock option gains from public companies. PREMERA pays a pro-rata portion of the annual and long-term incentives which is consistent with market practice.



PROPRIETARY MATERIAL REDACTED

Regardless, in PREMERA's plan – and most plans in general – CEOs and EVPs would likely qualify for full benefits under  PROPRIETARY MATERIAL REDACTED

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PROPRIETARY MATERIAL REDACTED

- Including SERP contributions and extending years-of-service is common practice, in our experience.
3. *PwC states that: "40% of the annual incentive award is determined based on achievement of non-financial performance criteria, a higher emphasis than typically found in best practice." (page 8)*

Towers Perrin Response:

- In our experience, annual incentive plans are based on performance measures that management and the board believe best reflect the tasks that should be accomplished in the current year. While these are often primarily financial, they may also include other measures that reflect the tasks needed to position the company for the future, which may or may not be heavily focused on financial results. Non-financial measures are, we believe, particularly relevant in the health insurance industry, as they represent the primary means to achieve adequate profitability, and include customer satisfaction, membership, retention and growth, service and quality.

It should be noted that PREMERA's annual incentive plan is structured in a somewhat unusual fashion, which actually puts more on financial results than is apparent at first. The plan in effect is funded entirely by financial results, and subsequently adjusted for performance in the major operating units and by growth in Membership and Business Unit quality measures.

4. *PwC states that: "Funding of the 2002 annual incentive plan begins upon achievement of a level of operating income that was well below prior years' actual operating income results and 2002 target operating income. Typically, funding thresholds are set commensurate with prior years' results and more closely aligned with the current year's financial plan." (Page 8)*

Towers Perrin Response:

- PREMERA's plan is entirely funded by profit, but is intended to allow some payment for achievement of membership and business goals provided profit achieves a minimal level. The PwC statement is technically correct as related to a conventional additive incentive plan design that pays out for performance in distinct categories, e.g., corporate, business unit, individual, financial, strategic, etc., but is not accurate regarding PREMERA's plan. In the more conventional arrangement, if one category fails to hit threshold, the other(s) can still pay out.

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Therefore, the *results* of the PREMERA plan are similar to those of more typical designs.

Additionally, it is the targeted performance, and less so the range around target, that is important. PREMERA targeted operating income growth in 2002 of about 16.5% over 2001 results (i.e., \$32.5 million target in 2002 compared to \$27.9 million results in 2001).

PROPRIETARY MATERIAL
REDACTED

5. ***PwC states that: PREMERA's deferred compensation "program includes a match of [] on mandatory deferrals (credited [] per year for four years). This practice is above market." (Page 13)***

PROPRIETARY MATERIAL
REDACTED

PROPRIETARY MATERIAL REDACTED

Towers Perrin Response:

PROPRIETARY MATERIAL
REDACTED

- This program requires a deferral of incentive awards in excess of [] of salary, and provides a Company match of up to [] of the mandatory deferral, awarded [] per year, provided the executive remains employed for the full four-year period.

PROPRIETARY MATERIAL
REDACTED

- Towers Perrin agrees that the mandatory deferral program is unusual, and we understand that []

PROPRIETARY MATERIAL REDACTED

Towers Perrin valued the deferral match in our calculation of PREMERA compensation vs. market, and found that it can add approximately 33% to the total mandatorially deferred compensation of senior executives if the executive remains for the full four years. The results of our competitive pricing, however, show no significant impact on competitive pay positioning, with aggregate pay levels generally at market median levels.

6. ***PwC states that: "The total number of supplemental retirement plans is above market practice" (page 13)***

Towers Perrin Response:

PROPRIETARY MATERIAL
REDACTED

- Towers Perrin believes that the total number of plans is not a relevant issue; rather, we suggest that total benefits be viewed in light of market practice. The PwC report indicates that the replacement percentages (i.e., percent of pre-retirement income supplied by the pensions) are [] for the CEO, [] for the EVPs, and [] for SVPs, on average. Based on recent Towers Perrin studies conducted for clients in similar businesses, ratios for non-profit organizations are in the 40-60% based on a 20-25-year career, with CEO ratios of up to 70% for older and/or long service executives.

PROPRIETARY MATERIAL
REDACTED

Further, we understand that PREMERA's benefit consultant (Watson Wyatt) has valued the programs at lower rates than cited by PwC. This would make the value lower than the market rates.

* * *

Conclusion:

In Towers Perrin's opinion, PwC criticized the design of PREMERA's compensation plans without substantiation, by focusing on plan components in isolation and failing to properly account for the net program results based on the combined effect of all components.

C) Post-Conversion Compensation

- 1. *Many of the "above market" factors cited in the PwC Report regarding post conversion relate to the limit of what PREMERA would be able to do if no restrictions are added. Factors include the restriction period, maximum number of the first authorization that can be granted, etc.***

Towers Perrin Response:

A detailed draft of an equity incentive plan has been provided to the OIC Staff. Towers Perrin has reviewed this plan and found it to be consistent with market practice among public companies including health insurance companies.

- It is our understanding that the number of options to be granted to executives have not been determined (which at this date is entirely reasonable), and further that PREMERA has made several commitments regarding limits on options that could be granted during the first two years following an IPO.
- PwC raises the possibility that PREMERA could make grants above market practice. Towers Perrin observes that such a possibility exists with *any* public company, but that the mainstream practice is that senior management and the board of directors ensure that option and share grants are made consistently with the company's compensation philosophy and with the intention of striking a balance between the interests of management and shareholders, while recognizing the then current market conditions, etc., facing the company.

* * *

Conclusion:

In our opinion the preliminary plans and commitments as Towers Perrin understands them, in combination with our understanding of management's intention and the Compensation Committee's oversight, will make the post-conversion arrangements competitive and consistent with appropriate IPO grants at the outset of public ownership.

III. POST-CONVERSION COMPENSATION

Towers Perrin has reviewed documentation prepared to date regarding compensation plans post-conversion and IPO, including the Mercer report of October 17 proposing an equity-based compensation strategy.

The following summarizes our comments regarding various aspects of the post-conversion program.

Equity Incentive Plan adopted by the Board

The draft equity incentive plan is an "omnibus plan" of a type frequently adopted at IPO. It provides broad latitude to the Compensation Committee to craft and grant various types of equity-based incentive programs within the parameters of Exhibit G-10 of Form A. Specific grant limits are set periodically without prescribed limits on individual award levels, vesting terms, etc. Towers Perrin generally recommends that this type of plan be adopted at the outset of public ownership as it provides flexibility to tailor future programs in accordance with changes in strategy, tax and legislative factors, recruiting needs, etc.

An omnibus plan carries the implicit understanding that the Board and its Compensation Committee will act responsibly in granting awards consistent with the company's articulated and approved compensation philosophy, and also with the need to protect shareholder interests. On this latter point, it should be noted that as a public company, most aspects of equity-based compensation are fully disclosed to shareholders (and the public), who have become increasingly vocal in their concern regarding "excessively" generous or dilutive equity awards.

As noted in the PwC report, the initial share reserve of 7% is consistent with competitive practice. PREMERA's agreement to limit grants to executives in the first year to a maximum of 2.8% is also appropriate in our opinion to provide flexibility at the date of grant. We observe that some companies grant options the first year of public ownership at a "normal" annual rate, while other organizations make larger-than-normal grants the first year (often followed by *no* grants in the following year) in order to "jump start" the alignment between management and shareholders through share ownership. We understand that final proposed grants have not been established.

Mercer Outline of Proposed Program

Mercer outlined an approach to implementing the equity-based program to the PREMERA Compensation Committee and to the Board of Directors on October 17, 2003. This program contains several notable recommendations:

- Elimination of the mandatory deferral program. Towers Perrin concurs, as the plan appears to have limited value as either a retention or incentive device.

- No changes in the AIP or LTIP. Towers Perrin agrees, in order to retain the ability to determine incentives (partly) by financial, strategic, and other measures that recognize PREMERA's focus on its insureds and providers, as well as shareholders through the stock-based program.
- Substitution of shares for cash in the LTIP. This approach blends the interests of all constituents in a single incentive program that is efficient compared to options in its use of shares. Because a share has a higher value than a single option, use of shares creates less dilution than options to deliver a target dollar value.
- Proposed individual option awards. The proposed grants are intended to bring total direct compensation in line with that of the median of the *blended* peer group, comprising both public and non-public companies. This is consistent with the Company's pre-conversion philosophy, which was not fully implemented because of the lack of stock options, and Towers Perrin concurs.
- Option terms were proposed that are consistent with best practices.
- Director compensation is proposed at the median of the peer group of public companies, which is appropriate in our opinion and consistent with best practices, as responsibilities and levels of compensation tend to differ substantially between public and private companies.

Blackstone Report of October 27, 2003

- The Blackstone report raises a number of questions regarding option terms that have subsequently been addressed.
- Certain proposed terms are compared unfavorably to other individual IPO situations, but the report does not cite instances where PREMERA is proposing terms inconsistent with general market practice.
- The report cites five mutual life companies that were prohibited from issuing options for *one year* following the IPO. Three of these companies are domiciled in New York, which has had a strict one-year limitation policy [based on precedent for many years]. Hancock did not allow option grants for one year but provided loans to purchase stock. Prudential allowed option grants to VPs and below after six months.

* * *

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Conclusion:

Towers Perrin believes that the proposed equity plans provide a reasonable level of flexibility to tailor an equity-based long-term incentive plan that is fair to executives and shareholders, and we have no reason to believe that the resulting program will result in unjust enrichment of PREMERA executives.

APPENDIX

Towers Perrin's Pricing of PREMERA positions:

PROCESS

Towers Perrin determined the target compensation opportunity for the PREMERA positions to be compared as follows:

- Annual base salary – the review date annual base salary
- Target (annual) total cash compensation (TTCC) – Annual base salary plus the target annual bonus percentage multiplied by the current annual base
- Target (annual) total direct compensation (TTDC) – TTCC plus:
 - a. The target long-term incentive percentage multiplied by the current annual salary
 - b. The portion of target annual and long-term incentive that exceeds [] of base salary multiplied by the [] 4-year annual crediting factor on mandatory deferrals, discounted 3% annually for the probability of receipt and discounted 5% annually for the time value of crediting

PROPRIETARY MATERIAL REDACTED

PROPRIETARY MATERIAL
REDACTED

Towers Perrin determined the compensation opportunity for the Competitive Market benchmark positions to be compared as follows:

- Annual base salary – the review date annual base salary
- Total (annual) cash compensation (TCC):
 - Survey - reported actual Total Cash Compensation
 - Proxy Peer group – the sum of reported salary and annual bonus
- Total direct compensation (TDC):
 - Survey - reported Actual Total Direct Compensation (LTI valued using annualized, expected value methodologies)
 - Proxy Peer group – the reported salary, annual bonus and the annualized expected value of long-term incentives are combined to determine TDC for the CEO and the remaining four reported executives. The non-CEO positions are grouped by rank order of 2nd highest through fifth highest to produce the relative benchmark matches, i.e., the second highest paid incumbent at PREMERA will be compared to the group of second highest paid proxy peer group executives.

Expected value of long-term incentives are determined as follows:

- *Cash Long-Term incentives* valued at present value of target payout discounted for risk of forfeiture
- *Restricted Stock* is valued at face value of shares granted and discounted for risk of forfeiture
- *Performance Stock* is valued at the face value of the target number of shares to be earned and discounted for risk of forfeiture
- *Stock Options* are valued using the Black-Scholes option pricing model to develop the expected value of the grant and then discounted for risk of forfeiture

All data is aged at 3.5% per annum to the review date (e.g., a survey effective date of March 2002 and a review date of January 2003 implies 10 months of aging or a 2.9% increase of the survey data points).

Based on incumbent specific responsibilities (as relayed by PREMERA management and representatives of the compensation committee and Board of directors) Towers Perrin compared the PREMERA EVP-CLO and PP position to a Chief Administrative Officer benchmark position to account for top responsibilities in multiple administrative disciplines (i.e., Legal, Human Resources, Public Policy, Internal and External Communications).

The benchmark compensation data is developed using a blend of appropriate survey source data (tabular or regression where appropriate - 80% weighting) and a specific proxy peer group (20% weighting).

Mercer Pricing of PREMERA positions:

PROCESS

Mercer Consulting determined the target compensation opportunity for the PREMERA positions to be compared as follows:

- Annual base salary – the review date annual base salary
- Target (annual) total cash compensation (TTCC) – Annual base salary plus the target annual bonus percentage multiplied by the current annual bonus
- Target (annual) total direct compensation (TTDC) – TTCC plus the target long-term bonus percentage multiplied by the current annual salary

Mercer Consulting determined the compensation opportunity for the Competitive Market benchmark positions to be compared as follows:

- Annual base salary – the review date annual base salary
- Total (annual) cash compensation (TCC):
 - Survey - reported actual Total Cash Compensation
 - Proxy Peer group – the sum of current reported salary and the 3-year average annual bonus as a percent of the respective year's salary applied to current salary.
- Total direct compensation (TDC):
 - Survey - reported actual Total Direct Compensation (LTI valued using annualized, expected value methodologies)
 - Proxy Peer group – the reported salary, 3-year average annual bonus and the 3-year average annualized expected value of long-term incentives (as a percent of the respective year's salary applied to current salary) are combined to determine TDC for the CEO and the remaining four reported executives. The non-CEO positions are grouped by rank order of 2nd highest through fifth highest to produce the relative benchmark matches, i.e., the second highest paid incumbent at PREMERA will be compared to the group of second highest paid proxy peer group executives.

Expected value of long-term incentives are determined as follows:

 - *Cash Long-Term incentives* valued at target payout if available, otherwise actual cash long-term payouts are used
 - *Restricted Stock* is valued at face value of shares granted

- *Performance Stock* is valued at the face value of the target number of shares to be earned
- *Stock Options* are valued using a Black-Scholes option pricing model to develop the expected value of the grant.

All data is aged at 4.1% per annum to the review date (e.g., a survey effective date of March 2002 and a review date of January 2003 implies 10 months of aging or a 3.4% increase of the survey data points).

Based on incumbent specific responsibilities (as relayed by PREMERA management and representatives of the compensation committee and Board of Directors) and scope differences in the surveys used, Mercer applied premiums or discounts to the benchmark position data.

The benchmark compensation data is developed using a blend of appropriate survey source data (tabular or regression where appropriate - 75% weighting) and a specific proxy peer group (25% weighting).

PricewaterhouseCoopers Consulting's Pricing of PREMERA positions:

PROCESS

PwC Consulting determined the target compensation opportunity for the PREMERA positions to be compared as follows:

- Annual base salary – the review date annual base salary
- Target (annual) total cash compensation (TTCC) – Annual base salary plus the actual bonus earned in 2002 (paid 2003)
- Target (annual) total direct compensation (TTDC) – TTCC plus the actual long-term incentive earned in 2002 (paid 2003)

PwC Consulting determined the compensation opportunity for the Competitive Market benchmark positions to be compared as follows:

- Annual base salary – the review date annual base salary
- Total (annual) cash compensation (TCC):
 - Survey - reported actual Total Cash Compensation
 - Proxy Peer group – Third party data provider (Equilar) - do not have the valuation methodology, PwC explains as base salary plus bonus
- Total direct compensation (TDC):
 - Survey – TCC plus long-term incentive multiples applied to competitive median and 75th percentile base salary levels. These percentages are discounted by 40% to “reflect PREMERA's private company status”
 - Proxy Peer group – Third party data provider (Equilar) - TCC plus long-term incentives using an average Black-Scholes option ratio applied to option grants, face value of restricted stock, and 3-year average of actual long-term incentive payouts

No mention of policy on aging data.

No adjustments mentioned based on incumbent specific responsibilities.

Premera

Competitive Base Salary Analysis - CEO & EVP's

Comparison to Mercer

Data in \$000's and updated to October 2003 by an annual factor of 3.5%.

Position Title	Premera		Competitive				% Difference			
	Incumbent	Base	Survey Position	25th %ile	50th %ile	75th %ile	25th %ile	50th %ile	75th %ile	
Towers Perrin Analysis										
President and CEO	Brereton Barlow	\$650	President / CEO	\$570	\$780	\$890	14%	-17%	-27%	
EVP, Chief Legal and Public Policy	Yori Milo	\$407	Top Administrative Services Executive	\$250	\$310	\$370	63%	31%	10%	
EVP, Chief Financial Officer	Kent Marquardt	\$300	Top Finance Executive	\$265	\$350	\$430	13%	-14%	-30%	
EVP, Chief Actuary	A. Wang	\$350	Top Actuarial Executive	\$200	\$235	\$265	75%	49%	32%	
Average Position				41%	12%	-4%				
\$ Weighted Average % Difference				33%	2%	-13%				

Mercer Analysis

President and CEO	Brereton Barlow	\$650	President / CEO	\$588	\$702	\$867	11%	-7%	-25%	
EVP, Chief Legal and Public Policy	Yori Milo	\$407	Top Legal Executive (with premium)	\$286	\$379	\$445	42%	7%	-9%	
EVP, Chief Financial Officer	Kent Marquardt	\$300	Top Finance Executive	\$206	\$277	\$343	46%	8%	-13%	
EVP, Chief Actuary	A. Wang	\$350	Top Actuarial Executive	\$189	\$222	\$265	85%	58%	32%	
Average Position				46%	17%	-3%				
\$ Weighted Average % Difference				35%	8%	-11%				

Percent Difference Towers Perrin vs. Mercer

President and CEO	Brereton Barlow	-3%	11%	3%	
EVP, Chief Legal and Public Policy	Yori Milo	-13%	-18%	-17%	
EVP, Chief Financial Officer	Kent Marquardt	29%	26%	25%	
EVP, Chief Actuary	A. Wang	6%	6%	0%	
Average Position		5%	6%	3%	
\$ Weighted Average % Difference		-1%	-6%	-2%	

Premera**Competitive Total Cash Compensation Analysis - CEO & EVP's****Comparison to Mercer**

Data in \$000's and updated to October 2003 by an annual factor of 3.5%.

Position Title	Premera		Competitive		% Difference		
	Incumbent	TTCC	Survey Position	25th %ile	50th %ile	75th %ile	75th %ile
Towers Perrin Analysis							
President and CEO	Brereton Barlow	\$1,040	President / CEO	\$825	\$1,540	\$2,505	-58%
EVP, Chief Legal and Public Policy	Yori Milo	\$570	Top Administrative Services Executive	\$345	\$515	\$560	2%
EVP, Chief Financial Officer	Kent Marquardt	\$420	Top Finance Executive	\$325	\$525	\$785	-46%
EVP, Chief Actuary	A. Wang	\$491	Top Actuarial Executive	\$270	\$325	\$435	13%
Average Position				51%	2%	-23%	
\$ Weighted Average % Difference				43%	-13%	-41%	

Mercer Analysis

President and CEO	Brereton Barlow	\$1,040	President / CEO	\$875	\$1,193	\$1,683	-38%
EVP, Chief Legal and Public Policy	Yori Milo	\$570	Top Legal Executive (with premium)	\$400	\$556	\$669	-15%
EVP, Chief Financial Officer	Kent Marquardt	\$420	Top Finance Executive	\$274	\$349	\$490	-14%
EVP, Chief Actuary	A. Wang	\$491	Top Actuarial Executive	\$235	\$326	\$396	24%

Average Position
\$ Weighted Average % Difference56% 15% -11%
41% 4% -22%**Percent Difference Towers Perrin vs. Mercer**

President and CEO	Brereton Barlow	-6%	29%	49%
EVP, Chief Legal and Public Policy	Yori Milo	-14%	-7%	-16%
EVP, Chief Financial Officer	Kent Marquardt	19%	50%	60%
EVP, Chief Actuary	A. Wang	15%	0%	10%

Average Position
\$ Weighted Average % Difference4% 18% 26%
1% -17% -24%

Premera**Competitive Total Direct Compensation Analysis - CEO & EVP's****Comparison to Mercer**

Data in \$000's and updated to October 2003 by an annual factor of 3.5%.

Position Title	Premera		Competitive			% Difference		
	Incumbent	TTDC	Survey Position	25th %ile	50th %ile	75th %ile	25th %ile	50th %ile
Towers Perrin Analysis								
President and CEO	Brereton Barlow	\$1,565	President / CEO	\$1,330	\$1,890	\$2,410	18%	-17%
EVP, Chief Legal and Public Policy	Yori Milo	\$769	Top Administrative Services Executive	\$590	\$800	\$1,020	30%	-4%
EVP, Chief Financial Officer	Kent Marquardt	\$567	Top Finance Executive	\$600	\$705	\$770	-6%	-20%
EVP, Chief Actuary	A. Wang	\$662	Top Actuarial Executive	\$315	\$490	\$605	110%	35%
Average Position				26%	-1%	-19%	26%	-8%
\$ Weighted Average % Difference								-26%

Mercer Analysis

President and CEO	Brereton Barlow	\$1,565	President / CEO	\$1,631	\$2,232	\$2,996	-4%	-30%	-48%
EVP, Chief Legal and Public Policy	Yori Milo	\$769	Top Legal Executive (with premium)	\$698	\$922	\$1,692	10%	-17%	-55%
EVP, Chief Financial Officer	Kent Marquardt	\$567	Top Finance Executive	\$595	\$760	\$1,498	-5%	-25%	-62%
EVP, Chief Actuary	A. Wang	\$662	Top Actuarial Executive	\$299	\$446	\$916	121%	48%	-28%
Average Position				31%	-6%	-48%	11%	-18%	-50%
\$ Weighted Average % Difference									

Percent Difference Towers Perrin vs. Mercer

President and CEO	Brereton Barlow	-18%	-15%	-20%
EVP, Chief Legal and Public Policy	Yori Milo	-15%	-13%	-40%
EVP, Chief Financial Officer	Kent Marquardt	1%	-7%	-49%
EVP, Chief Actuary	A. Wang	5%	10%	-34%
Average Position		-7%	-6%	-35%
\$ Weighted Average % Difference		14%	12%	48%

Premera**Competitive Base Salary Analysis - SVP's****Comparison to Mercer**

Data in \$000's and updated to October 2003 by an annual factor of 3.5%.

Position Title	Premera		Competitive		% Difference		
	Incumbent	Base	Survey Position	25th %ile	50th %ile	75th %ile	75th %ile
Towers Perrin Analysis							
SVP, Chief Actuary	Audrey Halvorsen	\$203	Top Actuarial Executive	\$200	\$235	\$265	2% -14% -23%
SVP, Human Resources	Barbara Magusin	\$160	Top Human Resources Executive	\$175	\$215	\$280	-9% -26% -43%
Service)	Karen Bartlett	\$208	Service Executive	\$175	\$205	\$250	19% 1% -17%
SVP - Chief Information Officer	Alan Smit	\$252	Top MIS Executive	\$260	\$295	\$350	-3% -15% -28%
CMO & SVP of Care Facilitation	John Castiglia	\$268	Chief Medical Officer / Medical Director	\$305	\$325	\$365	-12% -18% -27%
SVP Chief Underwriter	Sri Sagadevan	\$257	Top Underwriting Executive	\$140	\$165	\$205	84% 56% 25%
Mercer Analysis							
Average Position							2% -13% -28%
\$ Weighted Average % Difference							7% -6% -21%

SVP, Chief Actuary	Audrey Halvorsen	\$203	Top Actuarial Executive	\$189	\$222	\$265	7% -9% -23%
SVP, Human Resources	Barbara Magusin	\$160	Top Legal Executive (with premium)	\$181	\$214	\$255	-12% -25% -37%
Service)	Karen Bartlett	\$208	Service Executive	\$201	\$237	\$264	3% -12% -21%
SPV - Chief Information Officer	Alan Smit	\$252	Top MIS Executive	\$216	\$262	\$292	17% -4% -14%
CMO & SVP of Care Facilitation	John Castiglia	\$268	Chief Medical Officer / Medical Director	\$241	\$287	\$328	11% -7% -18%
SVP Chief Underwriter	Sri Sagadevan	\$257	Top Underwriting Executive	\$138	\$168	\$217	86% 53% 18%
Percent Difference Towers Perrin vs. Mercer							
Average Position							19% -1% -16%
\$ Weighted Average % Difference							16% -3% -17%

SVP, Chief Actuary	Audrey Halvorsen	6%	6%	0%
SVP, Human Resources	Barbara Magusin	-3%	0%	10%
Service)	Karen Bartlett	-13%	-14%	-5%
SPV - Chief Information Officer	Alan Smit	20%	13%	20%
CMO & SVP of Care Facilitation	John Castiglia	27%	13%	11%
SVP Chief Underwriter	Sri Sagadevan	1%	-2%	-6%
Average Position		6%	3%	5%
\$ Weighted Average % Difference		-7%	-3%	-5%

Premera

Competitive Total Cash Compensation Analysis - SVP's

Comparison to Mercer

Data in \$000's and updated to October 2003 by an annual factor of 3.5%.

Position Title	Premera		Competitive		% Difference		
	Incumbent	TTCC	Survey Position	25th %ile	50th %ile	75th %ile	%ile
Towers Perrin Analysis							
SVP, Chief Actuary	Audrey Halvorsen	\$284	Top Actuarial Executive	\$270	\$325	\$435	5% -13% -35%
SVP, Human Resources	Barbara Magusin	\$208	Top Human Resources Executive	\$215	\$315	\$455	-3% -34% -54%
Service)	Karen Bartlett	\$291	Service Executive	\$215	\$265	\$315	35% 10% -8%
SVP - Chief Information Officer	Alan Smit	\$353	Top MIS Executive	\$315	\$405	\$540	12% -13% -35%
CMO & SVP of Care Facilitation	John Castiglia	\$375	Chief Medical Officer / Medical Director	\$380	\$415	\$525	-1% -10% -29%
SVP Chief Underwriter	Sri Sagadevan	\$360	Top Underwriting Executive	\$180	\$225	\$270	100% 50% 33%
Average Position				12%	-12%	-33%	
\$ Weighted Average % Difference				19%	-4%	-26%	

Mercer Analysis

SVP, Chief Actuary	Audrey Halvorsen	\$284	Top Actuarial Executive	\$235	\$326	\$396	21% -13% -28%
SVP, Human Resources	Barbara Magusin	\$208	Top Legal Executive (with premium)	\$234	\$284	\$359	-11% -27% -42%
Service)	Karen Bartlett	\$291	Service Executive	\$229	\$303	\$326	27% -4% -11%
SPV - Chief Information Officer	Alan Smit	\$353	Top MIS Executive	\$300	\$359	\$456	18% -2% -23%
CMO & SVP of Care Facilitation	John Castiglia	\$375	Chief Medical Officer / Medical Director	\$303	\$372	\$436	24% 1% -14%
SVP Chief Underwriter	Sri Sagadevan	\$360	Top Underwriting Executive	\$156	\$229	\$317	131% 57% 14%

Average Position
\$ Weighted Average % Difference35% 2% -17%
28% 0% -18%

Percent Difference Towers Perrin vs. Mercer

SVP, Chief Actuary	Audrey Halvorsen	15%	0%	10%
SVP, Human Resources	Barbara Magusin	-8%	11%	27%
Service)	Karen Bartlett	-6%	-13%	-3%
SPV - Chief Information Officer	Alan Smit	5%	13%	18%
CMO & SVP of Care Facilitation	John Castiglia	25%	12%	20%
SVP Chief Underwriter	Sri Sagadevan	15%	-2%	-15%
Average Position		8%	3%	10%
\$ Weighted Average % Difference		-7%	-4%	-10%

Premera

Competitive Total Direct Compensation Analysis - SVP's

Data in \$000's and updated to October 2003 by an annual factor of 3.5%.

Position Title	Premera		Competitive			Comparison to Mercer		
	Incumbent	TTDC	Towers Perrin Analysis			% Difference		
			25th %ile	50th %ile	75th %ile	25th %ile	50th %ile	75th %ile
SVP, Chief Actuary	Audrey Halvorsen	\$384	\$315	\$490	\$605	22%	-22%	-37%
SVP, Human Resources (Service)	Barbara Magusin	\$281	\$325	\$440	\$790	-13%	-36%	-64%
	Karen Bartlett	\$393	\$255	\$280	\$305	54%	40%	29%
SVP - Chief Information Officer	Alan Smit	\$476	\$505	\$580	\$675	-6%	-18%	-29%
CMO & SVP of Care Facilitation	John Castiglia	\$506	\$655	\$740	\$835	-23%	-32%	-39%
SVP Chief Underwriter	Sri Sagadevan	\$485	\$270	\$300	\$335	80%	62%	45%

Average Position
\$ Weighted Average % Difference

14%
9%

-9%
-11%

-25%
-29%

Mercer Analysis

SVP, Chief Actuary	Audrey Halvorsen	\$384	Top Actuarial Executive	\$299	\$446	\$916	28%	-14%	-58%
SVP, Human Resources (Service)	Barbara Magusin	\$281	Top Legal Executive (with premium)	\$331	\$408	\$418	-15%	-31%	-33%
	Karen Bartlett	\$393	Service Executive	\$383	\$537	\$593	3%	-27%	-34%
SPV - Chief Information Officer	Alan Smit	\$476	Top MIS Executive	\$327	\$413	\$619	46%	15%	-23%
CMO & SVP of Care Facilitation	John Castiglia	\$506	Chief Medical Officer / Medical Director	\$421	\$546	\$836	20%	-7%	-39%
SVP Chief Underwriter	Sri Sagadevan	\$485	Top Underwriting Executive	n/a	n/a	n/a	n/a	n/a	n/a

Average Position
\$ Weighted Average % Difference

16%
20%

-13%
-10%

-37%
-38%

Percent Difference Towers Perrin vs. Mercer

SVP, Chief Actuary	Audrey Halvorsen	5%	10%	-34%
SVP, Human Resources (Service)	Barbara Magusin	-2%	8%	89%
	Karen Bartlett	-33%	-48%	-49%
SPV - Chief Information Officer	Alan Smit	54%	40%	9%
CMO & SVP of Care Facilitation	John Castiglia	56%	36%	0%
SVP Chief Underwriter	Sri Sagadevan	n/a	n/a	n/a

Average Position
\$ Weighted Average % Difference

16%
-9%

9%
0%

3%
14%

Premera

Competitive Base Salary Analysis - CEO & EVP's

Data in \$000's and updated to October 2003 by an annual factor of 3.5%.

Position Title	Premera		Survey Position	Competitive			% Difference		
	Incumbent	Base		25th %ile	50th %ile	75th %ile	25th %ile	50th %ile	75th %ile
	Towers Perrin Analysis								
President and CEO	Brereton Barlow	\$650	President / CEO	\$570	\$780	\$890	14%	-17%	-27%
EVP, Chief Legal and Public Policy	Yori Milo	\$407	Top Administrative Services Executive	\$250	\$310	\$370	63%	31%	10%
EVP, Chief Financial Officer	Kent Marquardt	\$300	Top Finance Executive	\$265	\$350	\$430	13%	-14%	-30%
EVP, Chief Actuary	A. Wang	\$350	Top Actuarial Executive	\$200	\$235	\$265	75%	49%	32%
Average Position				41%	12%	-4%	33%	2%	-13%
\$ Weighted Average % Difference									

PriceWaterhouseCoopers Analysis

President and CEO	Brereton Barlow	\$650	President / CEO	n/a	\$575	\$775	n/a	13%	-16%
EVP, Chief Legal and Public Policy	Yori Milo	\$407	Top Legal Executive & EVP (Not COO)	n/a	\$290	\$370	n/a	40%	10%
EVP, Chief Financial Officer	Kent Marquardt	\$300	Top Finance Executive & EVP (Not COO)	n/a	\$300	\$385	n/a	0%	-22%
EVP, Chief Actuary	A. Wang	\$350	Top Actuarial Executive	n/a	\$230	\$280	n/a	52%	25%

Average Position
\$ Weighted Average % Difference

n/a 26% -1%
n/a 22% -6%

Percent Difference Towers Perrin vs. PwC

President and CEO	Brereton Barlow	n/a	36%	15%
EVP, Chief Legal and Public Policy	Yori Milo	n/a	7%	0%
EVP, Chief Financial Officer	Kent Marquardt	n/a	17%	12%
EVP, Chief Actuary	A. Wang	n/a	2%	-5%

Average Position
\$ Weighted Average % Difference

n/a 15% 5%
n/a -17% -7%

Premera

Competitive Total Cash Compensation Analysis - CEO & EVP's

Comparison to PwC

Data in \$000's and updated to October 2003 by an annual factor of 3.5%

Premera			Competitive			% Difference			
Position Title	Incumbent	TTCC	Survey Position	25th %ile	50th %ile	75th %ile	25th %ile	50th %ile	75th %ile
				Towers Perrin Analysis					
President and CEO	Brereton Barlow	\$1,040	President / CEO	\$825	\$1,540	\$2,505	26%	-32%	-58%
EVP, Chief Legal and Public Policy	Yori Milo	\$570	Top Administrative Services Executive	\$345	\$515	\$560	65%	11%	2%
EVP, Chief Financial Officer	Kent Marquardt	\$420	Top Finance Executive	\$325	\$525	\$785	29%	-20%	-46%
EVP, Chief Actuary	A. Wang	\$491	Top Actuarial Executive	\$270	\$325	\$435	82%	51%	13%
Average Position									
\$ Weighted Average % Difference				51%	2%	-23%	43%	-13%	-41%

PriceWaterhouseCoopers Analysis

President and CEO	Brereton Barlow	\$1,040	President / CEO	n/a	\$975	\$1,395	n/a	7%	-25%
EVP, Chief Legal and Public Policy	Yori Milo	\$570	Top Legal Executive & EVP (Not COO)	n/a	\$395	\$600	n/a	44%	-5%
EVP, Chief Financial Officer	Kent Marquardt	\$420	Top Finance Executive & EVP (Not COO)	n/a	\$405	\$570	n/a	4%	-26%
EVP, Chief Actuary	A. Wang	\$491	Top Actuarial Executive	n/a	\$315	\$415	n/a	56%	18%

Average Position \$ Weighted Average % Difference

				n/a	28%	-10%
				n/a	21%	-15%

Percent Difference Towers Perrin vs. PwC

President and CEO	Brereton Barlow	n/a	58%	80%
EVP, Chief Legal and Public Policy	Yori Milo	n/a	30%	-7%
EVP, Chief Financial Officer	Kent Marquardt	n/a	30%	38%
EVP, Chief Actuary	A. Wang	n/a	3%	5%

Average Position \$ Weighted Average % Difference

				n/a	30%	29%
				n/a	-28%	-30%

Premera

Competitive Total Direct Compensation Analysis - CEO & EVP's

Comparison to PwC

Data in \$000's and updated to October 2003 by an annual factor of 3.5%.

Position Title	Premera		Competitive		% Difference		
	Incumbent	TTDC	Survey Position	25th %ile	50th %ile	75th %ile	
Towers Perrin Analysis							
President and CEO	Brereton Barlow	\$1,565	President / CEO	\$1,330	\$1,890	\$2,410	18% -17% -35%
EVP, Chief Legal and Public Policy	Yori Milo	\$769	Top Administrative Services Executive	\$590	\$800	\$1,020	30% -4% -25%
EVP, Chief Financial Officer	Kent Marquardt	\$567	Top Finance Executive	\$600	\$705	\$770	-6% -20% -26%
EVP, Chief Actuary	A. Wang	\$662	Top Actuarial Executive	\$315	\$490	\$605	110% 35% 9%
Average Position				38%	-1%	-19%	
\$ Weighted Average % Difference				26%	-8%	-26%	

PriceWaterhouseCoopers Analysis

President and CEO	Brereton Barlow	\$1,565	President / CEO	n/a	\$1,745	\$3,075	n/a	-10%	-49%
EVP, Chief Legal and Public Policy	Yori Milo	\$769	Top Legal Executive & EVP (Not COO)	n/a	\$575	\$955	n/a	34%	-20%
EVP, Chief Financial Officer	Kent Marquardt	\$567	Top Finance Executive & EVP (Not COO)	n/a	\$620	\$900	n/a	-9%	-37%
EVP, Chief Actuary	A. Wang	\$662	Top Actuarial Executive	n/a	\$470	\$695	n/a	41%	-5%
Average Position				n/a	14%	-28%			
\$ Weighted Average % Difference				n/a	4%	-37%			

Percent Difference Towers Perrin vs. PwC

President and CEO	Brereton Barlow	n/a	8%	-22%
EVP, Chief Legal and Public Policy	Yori Milo	n/a	39%	7%
EVP, Chief Financial Officer	Kent Marquardt	n/a	14%	-14%
EVP, Chief Actuary	A. Wang	n/a	4%	-13%
Average Position		n/a	16%	-11%
\$ Weighted Average % Difference		n/a	-12%	17%

Premera

Competitive Base Salary Analysis - SVP's

Data in \$000's and updated to October 2003 by an annual factor of 3.5%.

Position Title	Premera		Competitive						% Difference		
	Incumbent	Base	Survey Position	25th %ile	50th %ile	75th %ile	25th %ile	50th %ile	75th %ile		
Towers Perrin Analysis											
SVP, Chief Actuary	Audrey Halvorsen	\$203	Top Actuarial Executive	\$200	\$235	\$265	2%	-14%	-23%		
SVP, Human Resources (Service)	Barbara Magusin	\$160	Top Human Resources Executive	\$175	\$215	\$280	-9%	-26%	-43%		
	Karen Bartlett	\$208	Service Executive	\$175	\$205	\$250	19%	1%	-17%		
SVP - Chief Information Officer	Alan Smit	\$252	Top MIS Executive	\$260	\$295	\$350	-3%	-15%	-28%		
CMO & SVP of Care Facilitation	John Castiglia	\$268	Chief Medical Officer / Medical Director	\$305	\$325	\$365	-12%	-18%	-27%		
SVP Chief Underwriter	Sri Sagadevan	\$257	Top Underwriting Executive	\$140	\$165	\$205	84%	56%	25%		

Average Position
\$ Weighted Average % Difference

2% -13% -28%
7% -6% -21%

PriceWaterhouseCoopers Analysis

SVP, Chief Actuary	Audrey Halvorsen	\$203	Top Actuarial Executive	n/a	\$210	\$260	n/a	-3%	-22%
SVP, Human Resources	Barbara Magusin	\$160	Top Legal Executive	n/a	\$205	\$255	n/a	-22%	-37%
Service)	Karen Bartlett	\$208	Service Executive	n/a	\$180	\$235	n/a	16%	-11%
SPV - Chief Information Officer	Alan Smit	\$252	Top MIS Executive	n/a	\$245	\$285	n/a	3%	-12%
CMO & SVP of Care Facilitation	John Castiglia	\$268	Chief Medical Officer / Medical Director	n/a	\$275	\$325	n/a	-3%	-18%
SVP Chief Underwriter	Sri Sagadevan	\$257	Top Underwriting Executive	n/a	\$160	\$230	n/a	61%	12%

Average Position
\$ Weighted Average % Difference

n/a 9% -15%
n/a 6% -15%

Percent Difference Towers Perrin vs. PwC

SVP, Chief Actuary	Audrey Halvorsen	n/a	12%	2%
SVP, Human Resources	Barbara Magusin	n/a	5%	10%
Service)	Karen Bartlett	n/a	14%	6%
SPV - Chief Information Officer	Alan Smit	n/a	20%	23%
CMO & SVP of Care Facilitation	John Castiglia	n/a	18%	12%
SVP Chief Underwriter	Sri Sagadevan	n/a	3%	-11%

Average Position
\$ Weighted Average % Difference

n/a 7%
n/a -11% -7%

Premera

Competitive Total Cash Compensation Analysis - SVP's

Comparison to PwC

Data in \$000's and updated to October 2003 by an annual factor of 3.5%.

Position Title	Premera		Competitive			% Difference		
	Incumbent	TTCC	Survey Position	25th %ile	50th %ile	75th %ile	25th %ile	50th %ile
Towers Perrin Analysis								
SVP, Chief Actuary	Audrey Halvorsen	\$284	Top Actuarial Executive	\$270	\$325	\$435	5%	-13%
SVP, Human Resources Service)	Barbara Magusin	\$208	Top Human Resources Executive	\$215	\$315	\$455	-3%	-34%
	Karen Bartlett	\$291	Service Executive	\$215	\$265	\$315	35%	10%
SVP - Chief Information Officer	Alan Smit	\$353	Top MIS Executive	\$315	\$405	\$540	12%	-13%
CMO & SVP of Care Facilitation	John Castiglia	\$375	Chief Medical Officer / Medical Director	\$380	\$415	\$525	-1%	-10%
SVP Chief Underwriter	Sri Sagadevan	\$360	Top Underwriting Executive	\$180	\$225	\$270	100%	60%
Average Position								
\$ Weighted Average % Difference				12%	-12%	-33%	19%	-4%

PriceWaterhouseCoopers Analysis

SVP, Chief Actuary	Audrey Halvorsen	\$284	Top Actuarial Executive	n/a	\$280	\$380	n/a	2%
SVP, Human Resources Service)	Barbara Magusin	\$208	Top Legal Executive	n/a	\$255	\$335	n/a	-18%
	Karen Bartlett	\$291	Service Executive	n/a	\$225	\$375	n/a	29%
SPV - Chief Information Officer	Alan Smit	\$353	Top MIS Executive	n/a	\$325	\$400	n/a	9%
CMO & SVP of Care Facilitation	John Castiglia	\$375	Chief Medical Officer / Medical Director	n/a	\$365	\$450	n/a	3%
SVP Chief Underwriter	Sri Sagadevan	\$360	Top Underwriting Executive	n/a	\$210	\$310	n/a	71%
Average Position								
\$ Weighted Average % Difference				n/a	16%	-16%	n/a	13%

Percent Difference Towers Perrin vs. PwC

SVP, Chief Actuary	Audrey Halvorsen	n/a	16%	14%
SVP, Human Resources Service)	Barbara Magusin	n/a	24%	36%
	Karen Bartlett	n/a	18%	-16%
SPV - Chief Information Officer	Alan Smit	n/a	25%	35%
CMO & SVP of Care Facilitation	John Castiglia	n/a	14%	17%
SVP Chief Underwriter	Sri Sagadevan	n/a	7%	-13%
Average Position				
\$ Weighted Average % Difference		n/a	17%	12%
		n/a	-15%	-11%

Premera

Competitive Total Direct Compensation Analysis - SVP's

Comparison to PwC

Data in \$000's and updated to October 2003 by an annual factor of 3.5%.

Position Title	Premera		Competitive		% Difference		
	Incumbent	TTDC	Survey Position	25th %ile	50th %ile	75th %ile	
Towers Perrin Analysis							
SVP, Chief Actuary	Audrey Halvorsen	\$384	Top Actuarial Executive	\$315	\$490	\$605	22% -22% -37%
SVP, Human Resources Service)	Barbara Magusin	\$281	Top Human Resources Executive	\$325	\$440	\$790	-13% -36% -64%
	Karen Bartlett	\$393	Service Executive	\$255	\$280	\$305	54% 40% 29%
SVP - Chief Information Officer	Alan Smit	\$476	Top MIS Executive	\$505	\$580	\$675	-6% -18% -29%
CMO & SVP of Care Facilitation	John Castiglia	\$506	Chief Medical Officer / Medical Director	\$655	\$740	\$835	-23% -32% -39%
SVP Chief Underwriter	Sri Sagadevan	\$485	Top Underwriting Executive	\$270	\$300	\$335	80% 62% 45%
Average Position							
\$ Weighted Average % Difference				14%	-9%	-25%	-25%
				9%	-11%	-29%	-29%

PriceWaterhouseCoopers Analysis

SVP, Chief Actuary	Audrey Halvorsen	\$384	Top Actuarial Executive	n/a	\$455	n/a	n/a	-16%	n/a
SVP, Human Resources Service)	Barbara Magusin	\$281	Top Legal Executive	n/a	\$455	n/a	n/a	-38%	n/a
	Karen Bartlett	\$393	Service Executive	n/a	\$455	n/a	n/a	-14%	n/a
SPV - Chief Information Officer	Alan Smit	\$476	Top MIS Executive	n/a	\$455	n/a	n/a	5%	n/a
CMO & SVP of Care Facilitation	John Castiglia	\$506	Chief Medical Officer / Medical Director	n/a	\$455	n/a	n/a	11%	n/a
SVP Chief Underwriter	Sri Sagadevan	\$485	Top Underwriting Executive	n/a	\$455	n/a	n/a	7%	n/a
Average Position								n/a	n/a
\$ Weighted Average % Difference								-7%	n/a
								-7%	n/a

Percent Difference Towers Perrin vs. PwC

SVP, Chief Actuary	Audrey Halvorsen	n/a	8%	n/a
SVP, Human Resources Service)	Barbara Magusin	n/a	-3%	n/a
	Karen Bartlett	n/a	-38%	n/a
SPV - Chief Information Officer	Alan Smit	n/a	27%	n/a
CMO & SVP of Care Facilitation	John Castiglia	n/a	63%	n/a
SVP Chief Underwriter	Sri Sagadevan	n/a	-34%	n/a
Average Position				n/a
\$ Weighted Average % Difference				11%
				-4%